CONNECTICUT ACADEMY OF SCIENCE AND ENGINEERING

TESTIMONY OF THE CONNECTICUT ACADEMY OF SCIENCE AND ENGINEERING
BEFORE THE GOVERNMENT ADMINISTRATION & ELECTIONS COMMITTEE OF THE CONNECTICUT GENERAL ASSEMBLY

MARCH 17, 2014

SENATE BILL 452: AN ACT IMPLEMENTING THE INITIAL FINDINGS OF THE DISPARITY STUDY

Senator Musto, Representative Jutila and members of the committee, my name is Rick Strauss, Executive Director of the Connecticut Academy of Science and Engineering (CASE). The following testimony is presented regarding Senate Bill 452: An Act Implementing the Initial Findings of the Disparity Study.

The Academy completed and reported on the results of Phase 1 of the Connecticut Disparity Study to this committee in September 2013. Additionally, the Legislative and Administrative Initiatives Section of Phase 2 of the Disparity Study (see attached) was delivered to the committee in January 2014. These reports provided a foundation for the proposed legislation.

The Academy used the study recommendations and suggestions from the referenced reports as a foundation for our review of SB-452. We look forward to working with you and others as you may require to assure that the provisions of the bill conform with the committee's intentions.

Thank you for your time and consideration.

Respectfully Submitted,

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LEGISLATIVE AND ADMINISTRATIVE INITIATIVES

This section of the Connecticut Disparity Study: Phase 2 report identifies recommended legislative changes to state statutes, including but not limited to C.G.S. §4a-60g regarding the Set-Aside Program for Small Contractors and Minority Business Enterprises, and administrative changes with a timeline for action based on the findings of the Connecticut Disparity Study: Phase I report, as follows:

- Proposed Changes for 2014: The first set of recommendations identifies suggested statutory changes to make the race-based aspect of the program meet the judicial test of *strict scrutiny*. Further, this section also identifies administrative changes.
- Additional MBE and WBE Opportunities Program Improvements: The next set of recommended changes involves both administrative and legislative changes for improving processes and streamlining the Small Business Enterprise Program (SBE Program) and the Minority Business Enterprise (MBE) and Women Business Enterprise (WBE) Program. It is suggested that this program be named the MBE and WBE Opportunities Program (hereinafter referred to as the MBE and WBE Program).
- Legislative Changes upon Completion of the Disparity Study: Finally, the last set of recommended legislative changes is intended for implementation upon completion of the Disparity Study.

In order for a race program to be effective, enforceable, and legally defensible, it must meet the judicial test of *strict scrutiny*. *Strict scrutiny* is the most rigorous form of judicial review that courts use to determine the constitutionality of certain laws that involve *suspect classifications* such as race, religion, and national origin.

To determine if a statute passes the *strict scrutiny* test, the courts have considered whether the government has a compelling interest in creating the law and, if so, whether the law is *narrowly tailored* to meet the need. The following are criteria used to determine if a race-based program meets the judicial standard of *narrowly tailored*:

- MBE program eligibility needs to be based on availability of companies located within the market area for contracting services that are *ready, willing, and able* to provide such services.
- A race-based program needs to be established as a goal-based program rather than as a set-aside
- Race-based program goals must be adjusted periodically to account for the changing effects of discrimination.

- A program should be subject to periodic evaluation to determine if there is a continuing need for it.
- Recipients of contract dollars must not be penalized for not meeting MBE goals, if *good faith efforts* were used to identify and engage eligible MBEs.
- The types of companies that are eligible for the preference need to be limited with respect to racial category and location in the area from which suppliers are usually drawn for the contracting agency. The aim of the program is to correct discrimination that has placed MBEs at an economic disadvantage.

Further, gender-based programs are sometimes held to the same *strict scrutiny* requirement as race-based programs. However, some courts have used *intermediate scrutiny*, a less stringent form of judicial review, to evaluate gender-based programs on the basis that gender is not a suspect classification. The Supreme Court has not developed a framework for analyzing equal protection challenges to gender-based programs and whether such programs should be subject to the lesser constitutional standard of *intermediate scrutiny*. Therefore, it is recommended that the state meet the rigors of the *strict scrutiny* standard for implementing the MBE and WBE Program.

PROPOSED CHANGES FOR 2014

This section outlines the changes that are recommended for adoption during the 2014 legislative session. It also identifies recommended administrative changes that do not require legislation. The recommended legislative changes are intended to more closely align the MBE and WBE Program with the legal standards mentioned above.

Legislative Changes

Separate the programs. The first *statutory* change would be to separate the SBE Program, inclusive of nonprofits, from the MBE and WBE Program (C.G.S. §4a-60g), as the SBE Program is not held to the *strict scrutiny* standard. Therefore, the programs should be separated in order to align with judicial standards.

Goal-based program. The next step in aligning the MBE and WBE Program with judicial standards is to establish the MBE and WBE Program as goal-based rather than a set-aside program.[1] However, the SBE Program can remain a set-aside program since it is not based on race or gender; whereas the MBE and WBE Program must be established as a goal-based

[1] The language in the statutes will have to be amended to refer to the goal-based program as opposed to a set-aside when referring to the MBE and WBE Program. This includes but may not be limited to: C.G.S. § 4a-60g; 4a-60h; 4a-62; and 4a-52a.

program (see recommendation under administrative changes for implementation of a goal-based program).

The current statutory language under C.G.S §4a-60g(c) states:

> the total value of such contracts or portions thereof to be set aside by each such agency shall be at least twenty-five per cent of the total value of all contracts let by the head of such agency in each fiscal year, provided that neither: (1) A contract that may not be set aside due to a conflict with a federal law or regulation; or (2) a contract for any goods or services which have been determined by the Commissioner of Administrative Services to be not customarily available from or supplied by small contractors shall be included. Contracts or portions thereof having a value of not less than twenty-five per cent of the total value of all contracts or portions thereof to be set aside shall be reserved for awards to minority business enterprises.

Race- and gender-based programs that have been established as set-asides have not been upheld in court. Therefore, it is recommended Connecticut amend the statutory language to clarify that the state's MBE and WBE Program is established as a goal-based program.

Revising the statute to clearly define the MBE and WBE Program as a goal-based program will meet the judicial standard of *narrowly tailored*. As set forth in legal precedence, the courts have indicated programs must allow for flexibility by encouraging - through goals as opposed to set-asides - rather than requiring, contractors to use MBE and WBEs; and by providing waivers to contractors that are unable to meet the goals but can substantiate their *good faith efforts*.

The statute currently sets aside 25% of state contracting dollars for SBEs and 25% of that total is set aside for MBEs and WBEs. Therefore, in actuality, 18.75% is partitioned for SBEs and 6.25% for MBEs and WBEs. Since the recommended revisions to the statute separate the SBE Program and MBE and WBE Program, contract dollars for the SBE Program will be separate and distinct from contracting dollars for the MBE and WBE Program.

Therefore, it is recommended that the SBE Program set-aside be established at 18.75% of eligible contracting dollars and the MBE and WBE Program goal be established at 6.25% of eligible contracting dollars. This would keep the program percentages of eligible contracting dollars consistent with the current statute except that the MBE and WBE Program will be a goal-based as compared to a set-aside program. These percentages would remain in place in statute until the Disparity Study is completed.

Once the Disparity Study is complete, the statutes should be amended to provide for MBE and WBE Program goals to be established administratively based on the results of the statistical analysis of the Disparity Study and future disparity studies. See section on "Legislative

Changes Upon Completion of the Disparity Study" for additional guidance. Program goals should not be specified in statute; rather, the statute should require that program goals be set administratively. Additionally, this will provide an opportunity to modify program goals periodically between disparity studies based on interim statistical analyses, if necessary.

Interim goals. In addition, until completion of the Disparity Study, the MBE and WBE Program goal should be established in statute on an interim basis only (C.G.S. §4a-60g). Once the Disparity Study is completed, legislation should be adopted to provide for program goals to be established by administrative action based on the statistical determination of whether there is a disparity in the state contracting market, and hence discrimination. The section that follows on "Legislative Changes Upon Completion of the Disparity Study," provides additional information on establishing program goals and eligibility, including establishing separate goals for MBEs and WBEs.

Out-of-state firms. Since the market for contracting services extends beyond state borders, based on judicial precedence, the MBE and WBE Program must be representative of the market. This does not impact the state's SBE Program, which is an economic development program for Connecticut businesses and not a race- or gender-based program. The purpose of the MBE and WBE Program is to eliminate discrimination in state contracting. Therefore the program must allow MBEs and WBEs that are located in the geographic market (which could extend outside of Connecticut) for a particular industry or service to have the opportunity to participate in the program.

Currently the statutory (C.G.S. § 4a-60g) definition of "minority business enterprise" does not require a firm to be located in Connecticut, whereas the requirement for a firm to be located in Connecticut only applies to the definition of "small contractor." Therefore, once the SBE Program, and the MBE and WBE Program are separated statutorily, the statutes need to be amended to provide for out-of-state firms to be eligible for MBE and WBE certification, which will provide those firms with an opportunity to participate in the MBE and WBE Program.

Administrative Changes

Implementation of goal-based MBE and WBE Program. Assuming the SBE Program and the MBE and WBE Program are separated, guidelines on implementing the two programs need to be established. It is recommended that goals for contracts be published as part of the bid/proposal process so contractors are made aware of the goals for a particular project. Under these programs, a firm's work on a contract cannot be double counted to achieve both the MBE and SBE goals. However, it is suggested that the state examine goal setting to determine if the dollars paid to a particular firm can be separated and applied to more than one program goal on a contract.

Good faith efforts. In order to meet the judicial standards of a program being *narrowly tailored*, a race- and gender-based program must not penalize recipients of contract dollars for not meeting MBE and WBE goals, if *good faith efforts* were used by a prime contractor to identify and utilize eligible MBEs and WBEs. Connecticut grants waivers for *good faith efforts*; however, the state does not have an established standard that is used by all agencies and branches of state government for determining the level of effort and documentation that constitutes a prime contractor's *good faith effort*. Anecdotal information gathered in Phase 1 of the Disparity Study from contractors suggests that there is a lack of clarity concerning what constitutes a contractor's *good faith effort* and that the state's determination of such efforts seems arbitrary. Therefore, a standard must be established so that the *good faith efforts* of prime contractors to engage MBEs and WBEs can be fairly determined by the state and the contractors will have clarity in what is meant by *good faith effort*.

Self-performance (C.G.S. § 4a-60g(e)). Currently, DAS provides guidance on its website regarding the interpretation of the self-performance requirement. However, there is confusion within the contracting community concerning the requirements under this section of the statute. The self-performance requirement is critical to ensure MBEs and WBEs are not serving as pass-through entities. Therefore, it is suggested that DAS further clarify the statute, provide more examples of how to apply it under multiple circumstances and work with procurement staff in all branches of government to ensure consistent application.

Reciprocity. Since out-of-state firms will be able to participate in the MBE and WBE Program, based on the legislative recommendation in the previous section, DAS should consider the steps necessary to enter into reciprocity agreements with other states as appropriate, based on proximity to the state and similarity of certification processes. Entering into reciprocity agreements will help facilitate Connecticut MBE and WBE certified firms in seeking work in other states.

Through engaging other state's certification offices, Connecticut can gain an understanding of the differences in certification requirements and enforcement practices. However, one potential obstacle to entering into reciprocity agreements is the fact that the state does not proactively investigate whether firms legitimately match the certification for which they apply by conducting unannounced on-site visits. Other states may be hesitant to enter into agreements knowing that Connecticut's MBE and WBE certified firms have not been adequately vetted. For example, all contracting, engineering, and architectural firms in Massachusetts applying for certification under the state program receive an on-site visit while other industries receive a phone call. It was noted in the Disparity Study-Phase I report, based on the research conducted, that the DAS reported that additional staff resources would be needed to conduct on-site visits. Therefore, in order to conduct certification compliance work, it is expected that DAS would need to allocate additional staff resources to conduct these activities.

ADDITIONAL MBE AND WBE OPPORTUNITIES PROGRAM IMPROVEMENTS

These recommended changes, based on the research conducted in Phase I of the Disparity Study, are intended to improve the MBE and WBE Program, either through streamlining it with the federal DBE program or by adding transparency.

Legislative Changes

Definition of small business. Since the programs will be separated into an SBE Program and the MBE and WBE Program, consideration should be given as to whether or not a business will also have to be economically disadvantaged to qualify for the MBE and WBE Program. Consideration should be given to whether establishing a small business size threshold and criteria for the threshold would be beneficial for the program and if so, whether it should be based on the current definition, which is defined as a company having annual gross revenues not exceeding $15 million, or a net worth test.

The Disparity Study - Phase I report recommends changing the definition of a small business for the MBE and WBE Program. The rationale for the change is to make the definition more specifically tailored to provide opportunities to businesses that are economically disadvantaged. For example, the definition does not take into account industry differences. Businesses in industries that require large capital investment such as heavy construction may warrant a larger revenue cap than businesses in the service industry. Further, using annual gross revenues as a measurement does not necessarily identify businesses with economic disadvantages. Rather, a net worth test is a more appropriate measurement tool.

Three options for changing the definition of "small business" for the MBE and WBE Program in an effort to ensure fair representation of the types of small businesses that exist in the market that should be considered are as follows:

1) Make the MBE and WBE Program size limit the same as the federal DBE program;
2) Change the MBE and WBE Program size limit to net worth; and/or
3) Have different definitions depending on the industry for which services are utilized.

These options will be further analyzed, with more specific recommendations for establishing separate definitions for size limits for SBEs, and MBEs and WBEs.

Self-performance (C.G.S. § 4a-60g(e)). During the 2013 Legislative Session, P.A. 13-304 increased the percentage of work required to be performed by any prime SBE/MBE company that is awarded a contract under the set-aside statute. Following are the new guidelines as published on the DAS website:

Previously, a company awarded a set-side contract was required to self-perform at least 15% of such contract; it will now be required to self-perform at least 30%. Further SBEs and MBEs that subcontract some of the work under their set-aside contracts will be required to subcontract at least 50% of the remaining work (i.e., the work not self-performed by the prime) to SBEs and MBEs, respectively, instead of 25%, under current law. Please note the 50% requirement applies to the work subcontracted; in other words, the percentage to be self-performed by the prime contractor cannot be used to accomplish the 50% requirement.

For example, if an SBE is awarded a $100,000 state contract under the set-aside statutes, that SBE will be required to perform at least $30,000 of the work under the contract. If the SBE self-performs $30,000 of the work, and chooses to subcontract the remainder, the SBE must subcontract at least $35,000 of the work to another certified SBE (50% of the remaining $70,000 on the contract).

Adding a second goal to contracts further complicates the effective management and administration of the program. The self-performance requirement is critical to ensure MBEs and WBEs are not serving as pass-through entities. However, the decision to subcontract and with whom to subcontract should only be a business decision of the MBE or WBE. However, contractors awarded contracts as part of the separate SBE Program should not be excluded from using *good faith efforts* to engage MBEs or WBEs for work on such contracts when appropriate based on the type and scope of work of such projects. It is recommended that this legislative action should be taken as soon as possible.

Affirmative Action Plans. The recommendations in this section concerning the Affirmative Action Plan include both legislative and administrative actions.

It is recommended that the plan be split into two parts:

- Affirmative Action Plan: This part of the plan would include the general policy statement, internal and external communications, and company workforce and organization analysis.
- MBE and WBE Utilization Plan for contracts, when required: This part of the plan would include contract specific information regarding MBE and WBE utilization (also applicable for SBE utilization for the SBE Program) on contracts, when required (Currently Section 11: Subcontractor Availability Analysis and Section 12 Minority Business Enterprise Goals and Timetables in the Affirmative Action Plan).

For the state MBE and WBE Program, companies submit the existing Affirmative Action Plan for each contract, when required. However, for the federal DBE Program administered by

ConnDOT, companies must submit the Affirmative Action Plan only every two years. The state's requirement creates an administrative burden, with plans potentially not being approved in a timely manner due to resource constraints. Therefore, it is recommended that the state adopt the practice utilized by ConnDOT for the federal DBE Program and have the Affirmative Action Plan submitted every two years. This will not only create consistency for the contracting community, but it will also alleviate the administrative burden and allow the administrative focus for each contract to be on the MBE and WBE Utilization Plan.

Another consideration is who should have responsibility for approval and monitoring of the MBE and WBE Utilization Plans. ConnDOT has a Memorandum of Understanding (MOU) with the Commission on Human Rights and Opportunities (CHRO) that provides them with authorization to approve and monitor Utilization Plans for companies for the federal DBE program. This model could be considered for state agencies/branches of state government by establishing MOUs that provide agencies contracting for services the authority to approve and monitor these plans.

Another option would be to amend the state statutes to provide contracting authorities with the responsibility for the approval and monitoring MBE and WBE Utilization Plans. However, a review of options should include an analysis of personnel resources necessary for implementation.

Further, in an effort to more seamlessly integrate the MBE and WBE Program into the bid/contracting process, it is recommended that the MBE and WBE Utilization Plan be submitted prior to contract execution, when such plans are required. This will provide an opportunity to assess the utilization of MBE and WBE firms during the contracting process. Wherever approval of the utilization plans resides, it is important that such approval occur within a predetermined time period so as not to delay the execution of a contract.

Uniformity. It is suggested that consideration be given to streamlining the certification process for all program classifications. Several options, among others, to consider include:

- Create a single certification office that is responsible for all state program certifications including the MBE and WBE Program, SBE Program, federal DBE program administered by ConnDOT, and the federal DBE Program for meeting EPA requirements. Contractors would be able to select the certifications that they would like to apply for through a single application process, rather than having to apply separately for the federal DBE and state programs.
- Adopt the federal DBE program certification requirements for the state's MBE and WBE Program.

Municipalities. Currently, municipalities are excluded from participating in the program. However, a sizeable amount of state funding is provided to municipalities for projects that are contracted for by municipalities. To ascertain whether there is discrimination in the state contracting marketplace, pass-through state funding to municipalities should be included in the MBE and WBE Program. Therefore, it is recommended that the exclusion that exempts state-funded municipal projects from the MBE and WBE Program should be eliminated. However, this legislative change has not succeeded in the past when considered by the General Assembly. Therefore, it is recommended that this be explored in greater depth before a legislative recommendation is proposed.

Administrative Changes

Commercially useful function. The term "commercially useful function" refers to contract dollars that go towards activities in a project that provide an added value. For example, the trucking of materials provides a service, or added value, but the purchasing of the material being hauled on behalf of a prime contractor may not necessarily be considered a "commercially useful function" depending on the specifics of the contract and contractors involved. Since determining a commercially useful function is complex, this issue will be researched in greater detail before submitting a recommendation for consideration.

Program administration, compliance, and enforcement. The anecdotal research of the Disparity Study - Phase I report, including findings from interviews, surveys, and focus group sessions, identified the need for a more streamlined and transparent process for administration, certification, compliance, and enforcement. The findings indicated there was fragmentation, differences by state agency in program implementation, and a lack of transparency for determining *good faith efforts*. To help provide consistency to the contracting community, the state should consider ways to provide a more centralized approach, with clear program leadership that has overall accountability for the SBE Program and the MBE and WBE Program. Determining the best organizational structure for program administration, certification, compliance, and enforcement that provides consistency for the contracting community will be analyzed and a recommendation will be made based on best practices across the country.

LEGISLATIVE CHANGES UPON COMPLETION OF THE DISPARITY STUDY

Evidence-based goals. Once the Diversity Data Management System is operational, the state will have the mechanism for collecting contractor and subcontractor contracting information and payment data systematically and at a level of detail that will enable the study's econometric analysis to be conducted. If discrimination is found based on the analysis, goals will be established for race-based groups that are identified to be experiencing discrimination. The MBE goals will be aimed at alleviating discrimination experienced by minority groups. Further,

based on this analysis, a separate goal for WBEs will be established, if it is found that WBEs are also experiencing discrimination.

Sunset date. Since the purpose of the MBE and WBE Program is to eliminate discrimination in the marketplace, the program needs to be evaluated continuously to determine if the goals should be modified and if the appropriate groups are included in the program. Upon completion of the current Disparity Study, the program goals for the MBE and WBE Program should be removed from the statute with new goals set administratively. Additionally, the statute should be amended to include only those groups that will be included in the MBE and WBE Program. The goals and the groups that are included will then be evaluated administratively on an ongoing basis. Further, a sunset date should be established by statute that will coincide with the completion of the next disparity study. The process of sunsetting the program to coincide with the results of future disparity studies should continue until discrimination in the marketplace is eliminated.

CONCLUDING REMARKS

It is important to align the MBE and WBE Program with the judicial standards for a race- and gender-based program. Further, suggested administrative changes can help provide clarity for the contracting community and also streamline and create uniformity among the various state programs.